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Supreme Court of the United States

OCTOBER TERM, 1945

Supreme Court, U. S.
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No. 5

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY,
Petitioners,

vs.

UNITED STATES OF AMERICA.

BRIEF OF THE CITY OF NEW YORK AND NATIONAL INSTITUTE OF MUNICIPAL LAW OFFICERS, *AMICI CURIAE.*

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BRIEF OF CITY OF NEW YORK AND NATIONAL INSTITUTE OF MUNICIPAL LAW OFFICERS, *AMICI CURIAE.*

Preliminary Statement

This joint brief is submitted on behalf of the City of New York and by the National Institute of Municipal Law Officers on behalf of 415 municipalities throughout the country. The law officers of 12 of the country's leading cities have joined in the brief, as representatives of the 415 member cities of the Institute.

Questions Presented

The broad question asked by the Court is whether the Federal government may constitutionally tax any state property, activity or income. It is manifest that the question posed reaches down to and touches the very foundations of the constitutional structure of our country.

We propose to demonstrate that the proper answer to the question is that state property, activities and income,

regardless of their nature or source may not properly be taxed by the Federal government. We propose that this Court return to the basic doctrine of sovereign immunity of states from federal interference by taxation and reject the limitation upon that doctrine which lies in the theory adopted by the Court in deciding *South Carolina* v. *U. S.*, 199 U. S. 437 (1905), and those cases which have in one form or another restated the views expressed in that opinion.*

Outline of Argument

It is our intention in this Brief to demonstrate:

The doctrine of inter-governmental tax immunity is basic in our form of constitutional government. The immunity of State instrumentalities of government from Federal taxation and the immunity of the Federal instrumentalities of government from State taxation are necessarily reciprocal. This immunity proceeds from the circumstance that both the State and the Federal governments are sovereign in their spheres. The *South Carolina* case represents a departure from this principle; its rule is contrary to basic constitutional law and, as a necessary result, so confusing and lacking in precision as to require its abandonment.

Since Federal instrumentalities, regardless of their nature, are immune from State taxation so, under the Constitution, State instrumentalities, regardless of their nature, are similarly immune from Federal taxation.

We shall not consider here whether the Federal government may levy taxes upon incomes received by individuals from states and their instrumentalities nor shall we consider

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* Since the answer we propose to Question "1" framed by the Court in its order for reargument is an unqualified negative, we do not reach Question "2" for consideration. The answer to the latter question is implicit in that which we have made to the former.

whether persons receiving goods or services from states and their instrumentalities may be taxed upon them. These matters pose a problem not presented by the questions framed by the Court in this case.

ARGUMENT

The doctrine of inter-governmental tax immunity is basic in our form of constitutional government. The immunity of State instrumentalities of government from Federal taxation and the immunity of the Federal instrumentalities of government from State taxation are necessarily reciprocal. This immunity proceeds from the circumstance that both the State and the Federal governments are sovereign in their spheres. The *South Carolina* case represents a departure from this principle; its rule is contrary to basic constitutional law and, as a necessary result, so confusing and lacking in precision as to require its abandonment.

Since Federal instrumentalities, regardless of their nature, are immune from State taxation so, under the Constitution, State instrumentalities, regardless of their nature, are similarly immune from Federal taxation.

(1)

Prior to 1905 this Court repeatedly stated that state instrumentalities and their activities, regardless of their nature, were immune from federal taxation (*U. S.* v. *Railroad Company,* 17 Wall. 322 (1873) and cases cited; *Van Brocklin* v. *Tennessee,* 117 U. S. 151 (1886) and cases cited; *Veazi Bank* v. *Fenno,* 8 Wall. 533 (1869) and cases cited. See also Cooley on *Constitutional Limitations* (2 Ed.) pp. [532] *et seq.*, *U. S.* v. *Owens,* 100 Fed. 70 (D. C., E. D. Mo. 1900); *State* v. *Garten,* 32 Ind. 1 (1869)).

Similarly, this Court held, as it has done to this very day, that the converse of that proposition is true and that Federal instrumentalities and their activities are immune

from State taxation regardless of their nature. *McCulloch* v. *Maryland*, 4 Wheat. 316 (1819); *Maricopa County* v. *Valley Bank*, 318 U. S. 357 (1943) and cases cited; *Mayo* v. *U. S.*, 319 U. S. 441 (1943) and cases cited; *U. S.* v. *Allegheny County*, 322 U. S. 174 (1944) and cases cited; *Cleveland* v. *U. S.*, 323 U. S. 329 (1945) and cases cited.

Since *McCulloch* vs. *Maryland*, 4 Wheat. 316 (1819) the fundamental doctrine that the federal government is immune from state taxation and, reciprocally, the state governments are immune from federal taxation has never been questioned in principle.*

The foundation of the rule exempting states from federal taxation was stated by Mr. Justice NELSON in *Collector* vs. *Day*, 11 Wall. 113, 124-5 (1870):

> "The general government, and the States, although both exist within the same territorial limits, are separable and distinct sovereignties, acting separately and independently of each other, within their respective spheres. The former, in its appropriate sphere, is supreme; but the States within the limits of their powers not granted, or, in the language of the tenth amendment, 'reserved' are as independent of the general government as that government within its sphere is independent of the States. * * * Such being the separate and independent condition of the States in our complex system, as recognized by the Constitution, and the existence of which is so indispensable, that, without them, the general government itself, would disappear in the family of nations, it would seem to follow, as a reasonable, if not a necessary consequence, that the means and instrumentalities employed for carrying on the operations of their government, for preserving their existence, and fulfilling the high and responsible duties assigned to them in the Constitution, should be left free and un-

* Professor Powell points out that the doctrine of governmental immunity from taxation was generally, if not universally assumed long prior to the *McCulloch* case. *The Remnant of Tax Immunities*, 58 Harvard Law Review, at p. 787. See also cases cited in Cooley, on *Constitutional Limitations* (7 ed.) pp. 996-7, footnote 1.

> impaired, should not be liable to be crippled, much less defeated by the taxing power of another government, which power acknowledges no limits but the will of the legislative body imposing the tax."

As Judge COOLEY noted in *Constitutional Limitations* (2nd Ed.) p. [585]:

> "If the States possessed the authority to tax the agencies of the national government, they would hold within their hands a constitutional weapon which factious and disappointed parties would be able to wield with terrible effect when the policy of the national government did not accord with their views; while, on the other hand, if the national government possessed a corresponding power over the agencies of the State governments, there would not be wanting men who, in times of strong party excitement, would be willing and eager to resort to this power as a means of coercing the States in their legislation upon the subjects remaining under their control."

In *Pollock* vs. *Farmers Loan and Trust Co.*, 157 U. S. 429, 584 (1894), the rule was again reaffirmed in clear terms. Thus:

> "As the States cannot tax the powers, the operations or the property of the United States, nor the means which they employ to carry their powers into execution, so it has been held that the United States have no power under the Constitution to tax either the instrumentalities or the property of a State."

In *United States* v. *Railroad Company, supra*, this Court gave unqualified approval to the doctrine, saying (pp. 327-328):

> "The right of the States to administer their own affairs through their legislative, executive, and judicial departments, in their own manner through their own agencies, is conceded by the uniform decisions of this court and by the practice of the Federal government from its organization. This carries with it an

> exemption of those agencies and instruments, from the taxing power of the Federal government. If they may be taxed lightly, they may be taxed heavily; if justly, oppressively. Their operation may be impeded and may be destroyed, if any interference is permitted. Hence, the beginning of such taxation is not allowed on the one side, is not claimed on the other."

Chief Justice HUGHES in *Willcuts* v. *Bunn*, 282 U. S. 216, 224 (1930), characterized as a "familiar aphorism" the proposition stated in *Ambrosini* vs. *United States*, 187 U. S. 1, 7 (1902), "that as the means and instrumentalities employed by the General Government to carry into operation the powers granted to it are exempt from taxation by the States, so are those of the States exempt from taxation by the General Government."

After this fundamental principle had been continually acknowledged for almost a century, this Court, in *South Carolina* v. *U. S.*, 199 U. S. 437 (1905), departed from it and, for the first time, laid down a limitation upon the rule in so far as the immunity of states from federal taxation is concerned.

In *South Carolina* v. *United States*, the State adopted a law providing for a state monopoly of the sale of intoxicating liquor. Under the law, the State provided for the appointment of government agents to sell liquor at wholesale and retail in government-operated establishments. All proceeds of the operation of the establishments went to the State and the profits arising were divided between the State and its governmental subdivisions. A Federal statute provided that every establishment for the sale of liquor was required to be licensed and license tax fees were imposed upon such establishments by the Federal government.

The State, having paid the license tax charges for its establishments, sued in the Court of Claims to recover the

sums so paid, and upon the dismissal of its claim in that Court, appealed to the Supreme Court.

The Supreme Court (three of the Justices dissenting) affirmed the judgment of the Court of Claims.

This determination was founded upon the conclusion that the exemption of state agencies from Federal taxation applied only to those agencies which were "strictly governmental" in their nature, and did not extend to those activities of a state government which were, at the time of the adoption of the United States Constitution, those of an "ordinary private business" (pp. 461, 463). The Court reached its conclusion through reasoning which, we submit, does not stand up under analysis.

1. Proceeding by parity of reasoning from cases against municipalities arising in tort, Mr. Justice BREWER concluded that where a state agency engages in what is considered a "proprietary" activity, it loses its standing as a governmental instrumentality and becomes a private agency.

2. The only state agencies which were intended to be exempted from Federal taxation, said Mr. Justice BREWER, were those whose activities were regarded as "strictly governmental" at the time the Federal Constitution was adopted.

3. The tendency of the times, said Mr. Justice BREWER, was in the direction of state ownership of many hitherto private enterprises—a tendency which he seems to have regarded as destructive of the republican form of state government—and it was never contemplated that the state could, by such device, rob the Federal government of a very substantial part, if not all, its revenues. Mr. Justice BREWER seemed to be particularly impressed by the fact that the profits realized by the state from the operation of its liquor establishments were substantial, amounting to more than half a million dollars a year, and feared that "mingling the thought of profit with the necessity for regulation", states finding profit in such undertakings might en-

gage in them to the serious detriment of Federal tax revenues.*

The defects in the reasoning of the majority opinion are apparent upon mere inspection, as Mr. Justice WHITE, in his dissenting opinion, quickly demonstrated.

The suggestion that the State of South Carolina was, in its liquor-selling activities acting merely as a proprietor completely overlooked the fact that traffic in liquor is a common subject of state control because of the social consequences of its abuse. Moreover, and more important, to import into the field of taxation, where precision and definition are absolutely essential, the utter confusion prevailing in the field of tort in regard to the liability of municipalities for "proprietary" as distinguished from "governmental" activities, (see *Brush* v. *Commissioner*, 300 U. S. 352, 362, *et seq.* (1936); Borchard, *Government Liability in Tort*, 35 Yale Law Journal, 129, 229) could only serve to promote obscurity and uncertainty. To apply as a test for determining what state activities are immune from Federal taxation, the situation existing prior to 1787 would result in patent absurdity. *Home Building & Loan Assn.* v. *Blaisdell*, 290 U. S. 398, 442-3 (1933).

Almost every governmental activity has both a proprietary predecessor and a present day proprietary analogue. Indeed, the early history of this continent affords striking examples of this fact on a very broad scale in the charters of the Massachusetts Company, the Virginia Company, and the Hudson Bay Company. Those organizations,

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* It should be noted that at the time of the *South Carolina* case the Federal government did not have available to it the great sources of tax revenue made possible by the 16th Amendment in comparison with which tax revenues obtained from liquor sales sink to insignificance. The fears expressed by Mr. Justice BREWER in regard to the threat of the disappearance of Federal revenue sources seem, in the light of events, as groundless as his fears that municipal ownership of public utilities would result in the destruction of our republican form of government.

though proprietary in nature, were at the same time governmental in every sense of the term. Coming down to later Colonial times we find that police activities were originally performed by private watchmen and are even today performed by private detective agencies. Fire fighting was originally carried on by private volunteers and is aided even today by private salvage corporations supported by insurance companies. Although governmental water supply systems existed in the ancient world (See brief submitted by the City of New York in *Brush* v. *Commissioner, supra*), in this country private water companies preceded municipal water supply systems and many such companies still exist alongside municipal systems. The disposal of garbage has been, in some states, first governmental then proprietary then back again to governmental. The operation of ferry boat transportation services by the City of New York was a function granted to it by the Dongan Charter in 1686 and the Cornbury Charter in 1708, yet similar services have been and still are supplied by private companies (see *Benson* v. *The Mayor*, 10 Barb [N. Y.] 223 [1850]). The operation of piers and docks has long been a private endeavor in many places, yet New York City has had publicly owned docks and piers for more than two centuries and has during that time derived substantial revenues from wharfage (see *Benson* v. *The Mayor, supra; Radway* v. *Briggs*, 37 N. Y. 255 [1867]). Proprietary traction companies originally supplied transportation facilities to cities and, where they have not been displaced by municipal transportation systems in whole or in part, still operate alone or in concert with municipal systems. Private turnpike companies and canal companies originally provided roadways, toll bridges and canals, and except as they have been displaced by state, municipal, and national highways and bridges and by state and national waterways still continue to do so. Federal, state and municipal light and power systems in many communities have displaced or supplemented private utility companies. Federal and state agencies, supply needs formerly or concurrently

supplied by mortgage companies and insurance companies. Banking, which one might regard as a typically commercial enterprise, is and long has been performed by goverment instrumentalities. Indeed, we need not be reminded that it was the normal and usual commercial activities of the Bank of the United States which brought about *McCulloch* v. *Maryland, supra.* Many states and municipalities provide garbage disposal, housing, lodgings and airfields concurrently with private enterprises. Marketing agencies in one form or another have been supplied by state and federal instrumentalities for many years alongside proprietary agencies providing similar services. It is thus clear that the test of "usual", "normal", or "historical" function is in reality no test at all which can be precisely or even reasonably applied.

Neither is the fact that a state derives substantial revenue from its activities an appropriate determining factor in considering whether or not the rule of tax immunity applies. Mr. Justice WHITE, in his dissenting opinion, disposed of this contention in apt terms (p. 469):

> "The contention that because one government may have derived income from the exertion of its authority, therefore the other government has a right to do likewise, even if the agencies of the other government be thereby taxed, reduces itself to this: That the power to burden arises from the very condition which prevents the power from existing. If pushed to its logical conclusion, the far-reaching result of the proposition that wherever revenue is derived from an act by one government, therefore the other may burden the agent or instrumentality of the other may be readily illustrated. Take the National Government. If in the exercise of its ample authority to establish national banks a tax is imposed on such banks and a revenue derived, do the States thereby become entitled, without the consent of Congress, to tax banks? Take the Post Office Department. If by the carrying of the mails revenue is derived by the Government of the United States, are the States from that fact entitled to tax the instru-

mentalities employed by the Post-Office Department? Take the ocean transport service of the United States. If under given circumstances a charge is made for transportation, and hence a revenue is earned, may the States cripple that service by taxation?"

See also

Brush v. Commissioner, 300 U. S. 352 (1936).

Both adherents and opponents of reciprocal governmental tax immunity have criticized the *South Carolina* case and demonstrated its shortcomings (Julius Henry Cohen and Kenneth Dayton, *Federal Taxation of State Activities and State Taxation of Federal Activities*, 34 Yale Law Journal, 807-833; Alden L. Powell, *National Taxation of State Instrumentalities*, [Univ. of Illinois, 1936], Ch. V, and pp. 124, *et seq.*).

It is apparent from an examination of the cases since 1905 that this Court has recognized a conflict between the fundamental principle of state sovereignty and the views expressed in the *South Carolina* case. In an effort to resolve the conflict the Court has cast about for a theory which would preserve the principle of state sovereignty and at the same time permit federal taxation of some state activities. In describing the ambit of the field of state activities which is to be taxable by the federal government the Court has attempted to contrive various tests which would admit the principle of federal non-interference with state governmental affairs yet affirm the principle stated in the *South Carolina* case. This result cannot be achieved, because the two principles cannot exist together—they are mutually exclusive.

An examination of the various tests shows in each of them the seeds of a confusion and an illogic equal to that prevailing in the field of municipal tort liability to which we have adverted (*supra*, p. 8):

Shortly after the *South Carolina* case was decided, the Court, through an opinion of Mr. Justice WHITE in *Murray*

v. *Wilson Distilling Company*, 213 U. S. 151, 154 (1909), sought to limit the rule to the proposition that a state did not have power "to destroy a pre-existing right of taxation possessed by the Government of the United States".

In *Ohio* v. *Helvering*, 292 U. S. 360, (1934), the Federal Government sought to collect a federal license tax fee from the State of Ohio as a retail liquor dealer and a wholesale liquor dealer, the State having a liquor manufacturing and selling monopoly within its territory. The State, pointing to the *Murray* case, *supra*, argued that since the 18th Amendment had already deprived the Federal Government of the field of liquor vending as a source of tax revenue, the State when it entered that field upon the repeal of the 18th Amendment did not deprive the Federal Government of a "preëxisting right of taxation". This contention the Court rejected and, denying the claim of the State to immunity, held that it was bound by the decision in the *South Carolina* case, *supra*, saying (at p. 369):

> "If a state chooses to go into the business of buying and selling commodities, its right to do so may be conceded so far as the Federal Constitution is concerned; but the exercise of the right is not the performance of a *governmental function*, and must find its support in some authority apart from the police power. When a state enters the market place seeking customers it divests itself of its *quasi* sovereignty *pro tanto*, and takes on the character of a trader, so far, at least, as the taxing power of the federal government is concerned."

In *Helvering* v. *Powers*, 293 U. S. 214 (1934) a street railway and its properties were taken over by the State of Massachusetts to be operated publicly for a period of ten years, pursuant to an act of the Massachusetts Legislature and the consent of the company. Under the statute the railway was placed in charge of a Board of Trustees appointed by the Governor of the State with the advice and consent of the Council. The trustees were to be paid by the company; the stockholders of the company were to continue to receive dividends; and at the end of the term the property was to

revert back to private control. During the period of public operation the State and its municipalities were to provide funds to meet deficits arising out of the operation of the company. In these circumstances the Court held that the salaries of the trustees, although they claimed to be public officials, were subject to federal income tax. Chief Justice HUGHES, writing for the Court, based his conclusion upon the ground that the operation of a street railway, like the sale of liquor in the *South Carolina* case, *withdrew a field of taxation from the Federal Government;* was not a *"usual"* governmental activity, but a business enterprise and was, therefore, not immune from federal taxation.

It seems clear that, if it had so desired, the Court could have founded its conclusion in the *Powers* case upon the fact that the arrangements providing for state operation of the railway were in reality merely a statutory device for the endowment of the railway company by the State to the extent of the Company's deficits. However, instead of basing his conclusion upon that ground, Chief Justice HUGHES stated that, even if the State had taken over the company's equipment in its entirety, the State would, nevertheless, be subject to federal taxation upon the railway properties and operations.

In *U. S.* v. *California*, 297 U. S. 175 (1935), the question presented was whether a state owned railroad was subject to the Safety Appliances Act (45 U. S. C., Sections 2, 6). The Court held the State bound by the provisions of that Act in the operation of its railroad. The basis of the Court's determination was that the principle by which state instrumentalities are exempted from federal taxation do not apply by analogy as a limitation upon the federal government's power to regulate interstate commerce. However, in discussing the immunity of states from federal taxation, the Court, citing the *South Carolina* case and those which followed the theory of that case, said (p. 185):

> "Hence we look to the activities in which the states have *traditionally* engaged as marking the boundary of the restriction upon the federal taxing power."

In *Flint* v. *Stone Tracy Company*, 220 U. S. 107 (1910), this Court in considering whether two proprietary traction companies were subject to a corporation tax, discussed the general subject of the limitations placed upon state immunity from federal taxation by the *South Carolina* case. The Court said (p. 172):

> "It is no part of the *essential* governmental functions of a State to provide means of transportation, supply artificial light, water and the like. These objects are often accomplished through the medium of private corporations, and, though the public may derive a benefit from such operations, the companies carrying on such enterprises are, nevertheless, private companies, whose business is prosecuted for private emolument and advantage. For the purpose of taxation they stand upon the same footing as other private corporations upon which special franchises have been conferred."

Nevertheless, in *Brush* v. *Commissioner*, 300 U. S. 352 (1937), the Court concluded that an employe of a city water supply system was exempt from the federal income tax law upon the ground that the activities of such an instrumentality are governmental. Summing up the cases, Mr. Justice SUTHERLAND said (pp. 361-2):

> "The phrase 'governmental functions', as it here is used, has been qualified by this court in a variety of ways. Thus, in *South Carolina* v. *United States*, 199 U. S. 437, 461, it was suggested that the exemption of state agencies and instrumentalities from federal taxation was limited to those which were of a *strictly* governmental character, and did not extend to those used by the state in carrying on an ordinary private business. In *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 172, the immunity from taxation was related to the *essential* governmental functions of the state. In *Helvering* v. *Powers*, 293 U. S. 214, 225, we said that the state 'cannot withdraw sources of revenue from the federal taxing power by engaging in businesses which constitute a departure from *usual* governmental functions and to which, by reason of their

nature, the federal taxing power would normally extend.' And immunity is not established because the state has the power to engage in the business for what the state conceives to be the public benefit. *Idem.* In *United States* v. *California*, 297 U. S. 175, 185, the suggested limit of the federal taxing power was in respect of activities in which the states have *traditionally* engaged.

> "In the present case, upon the one side, stress is put upon the adjective 'essential', as used in the *Flint* v. *Stone Tracy* case, while, on the other side, it is contended that this qualifying adjective must be put aside in favor of what is thought to be the greater reach of the word 'usual', as employed in the *Powers* case. But these differences in phraseology, and the others just referred to, must not be too literally contradistinguished. In neither of the cases cited, was the adjective used as an exclusive or rigid delimitation. For present purposes, however, we shall inquire whether the activity here in question constitutes an essential governmental function within the proper meaning of that term; and in that view decide the case."

In *Helvering* v. *Gerhardt*, 304 U. S. 405 (1938), the Court in determining that the salary of an employe of the Port of New York Authority was not exempt from the federal income tax again stated through its majority opinion that the test of whether or not a state activity is immune from federal taxation depended in general upon whether the state activity sought to be taxed is "essential" to the preservation of the government.

In regard to this, Mr. Justice BLACK, in a concurring opinion, said (pp. 426-7):

> "Conceptions of 'essential governmental functions' vary with individual philosophies. Some believe that 'essential governmental functions' include ownership and operation of water plants, power and transportation systems, etc. Others deny that such ownership and operation could ever be 'essential governmental functions' on the ground that such functions 'could be carried on by private enterprise.' * * *

> There is not, and there cannot be, any unchanging line of demarcation between essential and non-essential governmental functions. Many governmental functions of today have at some time in the past been non-governmental. The genius of our government provides that, within the sphere of constitutional action, the people—acting not through the courts but through their elected legislative representatives—have the power to determine as conditions demand, what services and functions the public welfare requires."

In *Allen* v. *Regents*, 304 U. S. 439 (1938), the Regents of the University of Georgia were public officers appointed to administer and control the University. That institution is a State facility. The University conducted athletic contests for which the general public was charged admission fees. The Regents brought suit against the Federal Collector of Internal Revenue to enjoin him from enforcing the federal admission tax law against them. That law levied a tax upon admission tickets to exhibitions. The tax had been collected by the Regents, but withheld from the federal tax authorities. The Court held that the University was subject to the provisions of the statute. Although the Court might well have found the result reached by it by regarding the tax as a levy upon the person purchasing tickets and not a tax upon the state, Mr. Justice ROBERTS, writing the majority opinion, said (p. 451):

> "In the final analysis what we must decide is whether, by electing to support a government through the conduct of a business comparable in all essentials with those *usually* conducted by private owners, a State may *withdraw the business from the field of federal taxation.*"

Thus, the confusion occasioned by attempts to base tax exemption of state instrumentalities upon a determination of whether their activities are "proprietary" or "strictly governmental", "essentially governmental" "usual governmental" or "commercial" profit-making or non-profit

making, or whether, not being "normally" governmental, they tend to withdraw from the federal government an existing taxable enterprise or activity, is manifest from an examination of the decisions of this Court:

The test of "strictly governmental" activity as of 1787 (*South Carolina* v. *U. S., supra*), gave way to the test of whether the activity destroyed a "pre-existing right of taxation possessed by the Government of the United States" (*Murray* v. *Wilson Distilling Company, supra*). Such a test would obviously redound to the advantage of states engaged in an activity before that activity was taxed by the Federal Government over those states which did not enter the particular field until after the activity was taxed. Presently, that test was abandoned (*Ohio* v. *Helvering, supra*), and in its place the test again suggested was that used in tort cases against municipalities, i.e., taxability of a state enterprise to depend upon whether that activity was "proprietary" or "governmental" (*Flint* v. *Stone Tracy, supra*). Such a test threatened to import into the law of taxation all the confusion and absurdity that years of conflicting rules had accumulated in the law of municipal tort liability, and very soon that test, too, was abandoned (*Brush* v. *Commissioner, supra*). In the meantime, an alternative test was growing up in the opinions of the Court: that of whether the state activity under scrutiny was "essential" or "non-essential" to the support of government. (See *Helvering* v. *Gerhart, supra*). Such a test, too, must fail, since not only are the terms concededly inexact and indefinite (*Helvering* v. *Therrell*, 303 U. S. 218, 223 [1937]), but their judicial definition threatens to find analogies in the hopeless morass of the "proprietary" against "governmental" in the field of municipal tort law. Similarly the tests of "usual" governmental activity (*Powers* v. *Helvering, supra*) offered neither a guide nor a direction: what is "usual" for a government depends upon what the government of the particular state has done in the past.

What might be "usual" or "traditional" in one state might be unusual or novel in another; what might be "essen-

tially" governmental must depend upon who makes the test and when; what is "proprietary" might none-the-less be "usual", "essential" or "traditional", dependent upon the what, where and when of the activity under scrutiny. (See *supra* pp. 8-10). Yet clearly the Court does not intend to discriminate between states in regard to taxation.

It thus appears that the tests for determining state immunity from federal taxation exemplified by the *South Carolina* case and those which have followed it in principle are so confusing and lacking in precision as to make it impossible to predict with any fair degree of accuracy whether a state activity is to bear the burden of a federal tax. It is a patent truism that the basis of a tax must be readily recognizable and that exactitude in determining whether a tax is in fact to be imposed is a *sine qua non* of proper taxation. The detriment to states and their instrumentalities which arises from the confusion created by the doctrine of the *South Carolina* case is clear: States and their instrumentalities cannot foresee whether they are to be taxed upon a particular proposed activity. With taxation looming as a factor of major importance in the conduct of activities, a state and its instrumentalities should be in the position of being able to determine what activities it can engage in safely without being burdened by taxation. If federal taxation is to be imposed upon new activities of state instrumentalities, public ownership and operation of utilities, provision by a state of low cost housing for its residents, and many other services vital to the community would be discouraged if not rendered impossible, despite the fact that the provision of such facilities by the state is dictated by circumstances. (See Cohen and Dayton, *Federal Taxation of State Activities, supra*).

(2)

The difficulty which this Court has experienced in dealing with the principle expressed in the *South Carolina* case and the variations on that principle attempted in the

cases which have followed it (supra pp. 10-18) arises out of the circumstance that the cases are in direct conflict with a basic principle of our form of federal government: that the states are independent sovereignties within their proper sphere, and taxation of one sovereignty by another is destructive of the sovereignty of the one taxed. The Court has repeatedly declared its adherence to the principle that states and the federal government are sovereign within their Constitutional spheres, and immune, in general, from federal and state taxation, respectively. It has reiterated that the respective immunities of the governments are "reciprocal"; and has repeatedly stated that both immunities proceed from identical reasons. See *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514, 522 (1922); *Willcuts* v. *Bunn*, 282 U. S. 216, 224-5 (1931); *Burnet* v. *Jergins Trust*, 288 U. S. 508, 514 (1933). See also on the sovereignty of the States *Munn* v. *Illinois*, 94 U. S. 113 (1877); *Fifield* v. *Close*, 15 Mich. 505 (1867); *Ashton* v. *Cameron County*, 298 U. S. 513 (1936). It is indeed "a familiar aphorism" that it is just as important to protect states from federal encroachments upon their sovereignty as it is to protect the Federal government from the encroachment of the states upon its sovereignty. Yet, on the one hand this Court has time and again held that regardless of the nature of the transactions engaged in by the Federal government it is immune from state taxation (supra, p. 3) while on the other hand it has stated that the immunity of states from federal taxation depends upon the nature of the State's activity sought to be taxed (supra, pp. 6-16). It would seem too clear for discussion that the sovereignty of a state is far more interfered with by the taxation of one of its public utilities than the sovereignty of the Federal government would be interfered with by local taxation based in part upon the value of federal-owned machinery in the hands of a private contractor located on lands owned by such a person. Yet, applying the test of the *South Carolina* case to the former the State might be taxed by the Federal government, while the latter remains immune from state taxation. *United States* vs. *Allegheny County*, 322 U. S. 174 (1944).

Presumably, under the last cited case and others of similar import, if the Federal government were to enter the liquor dispensing business it would be immune from state taxation, despite the *South Carolina* case and notwithstanding that in so doing it withdrew from the states a source of revenue.

The suggestion made in some of the opinions that the "supremacy" clause of the Constitution places the two sovereignties' power to tax upon different levels (*Helvering* vs. *Gerhardt, supra; Graves* vs. *New York ex rel. O'Keefe*, 306 U. S. 466 [1938]) is adequately met in Petitioner's Brief on Reargument (pp. 33-4) and in the Brief of the States (pp. 7-9, 17). We need only point out here, as did Mr. Justice NELSON in *Collector* vs. *Day, supra*, that the supremacy clause applies only within the sphere of government delegated to the Federal Government and that sphere did not include the power to impinge upon State sovereignty through taxation. Within its own sphere a State is just as supreme as the Federal government is in its sphere.

The very existence of the theory of "supremacy" as a means by which the Federal government escapes state taxation upon activities identical with those which the Federal government taxes when engaged in by states, implies a recognition that state taxation upon Federal enterprises would seriously hamper Federal activities. Surely the converse of that proposition is true and States would be hampered just as seriously by Federal taxation. See *United States* vs. *Allegheny County, supra.*

Recognition of this basic illogic—to say nothing of unfairness*—is apparent in the attempts which this Court has made to expand the field of state tax immunity beyond the narrow limits laid down in the *South Carolina* case, in order to preserve a measure of state sovereignty, while at the same time endowing the Federal government with a

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*See Powell, *The Remnant of Tax Immunities*, 58 Harvard Law Review 757, at p. 804.

power to tax particular state activities (See pp. 14-15; *supra*). The two purposes, however, are mutually exclusive, since, as Chief Justice MARSHALL pointed out in the *McCulloch* case, the exercise of a power to tax a sovereignty is consistent only with the existence of a power to control that sovereignty. Despite some dissent (*Panhandle Oil Co.* v. *Knox*, 277 U. S. 218, 223 [1928]; *Graves* v. *New York, ex rel. O'Keefe, supra*, at p. 489) Marshall's picturesque phrase is still true: "The power to tax is the power to destroy". This the Court has often demonstrated. See, as an example, *Magnano Co.* v. *Hamilton*, 292 U. S. 40 (1933).

As long as the doctrine of the *South Carolina* case and the variations upon that doctrine offered in other cases are permitted to stand the difficulty will remain. Whether a state activity is or is not "governmental" or "essential" should in all logic depend upon whether the government of the State, acting under its own Constitution and statutes, determines that the activity is governmental or essential; *New York City Housing Authority* v. *Muller*, 270 N. Y. 333 (1936); *Puget Sound Power & Light Co.* vs. *Seattle*, 291 U. S. 619 (1934). See also dissenting opinion of Mr. Justice BRANDEIS in *New State Ice Co.* vs. *Liebmann*, 285 U. S. 262, 280 *et seq.* (1932) and concurring opinion of Mr. Justice BLACK in the *Gerhardt* case, *supra*.* Such a determination should not be left to the federal courts.

The underlying principle of reciprocal immunity from taxation enjoyed by the Federal government and the state governments is that the sovereignty of the governments must not be interfered with (*supra*, pp. 4-6). No argument is necessary to persuade this Court that the tax revenues of states cannot be subject to taxation by the Federal government. If they were, a direct interference with the

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* Indeed, such a suggestion is implicit in the statement of Mr. Justice MURPHY that any activity undertaken by the government is, for purposes of according tax immunity, "governmental." *Federal Land Bank* v. *Bismarck Co.*, 314 U. S. 95, 102 (1941).

states' sovereignty would occur. But taxes form only a portion of a state's revenue and the amount of such revenues is dependent upon both the needs of the state government and the availability to the state of other sources of revenue. The more sources of revenues apart from taxation which are available to state government, the less the state government is required to collect by taxation. If a state engages in activities which produce revenue, the amount required to be collected through the ordinary medium of taxation is proportionately reduced. Thus, when a state collects filing fees from litigants in its courts it is reducing the amount required to be obtained by taxation for the support of its judicial machinery. Similarly, if a state or one of its instrumentalities were to supply utility services to its residents without direct charge as they now supply education without direct charge, its tax collections would have to be increased, whereas if it supplied them at usual charges and those transactions resulted in gain to the state the state would be free to reduce its tax levies. Can it be said that in the one case the activity is "governmental" and in the other "proprietary"? Examples can be catalogued *ad infinitum*. To do so, however, would not change the obvious fact.

Thus, whether Federal taxation be imposed upon strictly governmental activities or imposed only upon the so-called proprietary activities engaged in by the states and their instrumentalities, the sovereignty of the states is directly impinged upon by the federal government. The difference between taxing the receipt of state taxes and taxing other revenues of the states and their instrumentalities is purely one of degree and amount and not one of principle.

The fundamental principle of our form of government is that the states are, except as otherwise expressly provided in the Constitution, separate sovereignties beyond the control of the Federal government (*supra*, pp. 4-6). If the Federal government is permitted to tax the states and their in-

strumentalities in any of their activities it would indirectly but nonetheless effectively control the kind of activities in which the states could engage. If, for example, the Federal government were to tax the gross receipts of a municipal transportation service, it might—no doubt would—render it impossible from a financial standpoint for the municipality to engage in such an activity (See testimony of Mayor LaGuardia in Hearings Before House Ways and Means Committee on Tax Exempt Securities, 76 Cong. 1st Sess. [1939], pp. 270 et seq.; see also testimony of Comptroller McGoldrick in *Commissioner* v. *Estate of Shamberg* and *Same* v. *Estate of White*, 323 U. S. 792 [1944] den. cert. 144 Fed. (2) 998, 1019 [C. C. A. 2, 1944]). Similarly, if this Court were to declare that municipally-owned services and utilities and the host of activities engaged in by municipal governments, apart from those which this Court has recognized to be strictly governmental, were subject to taxation, the right of the states and their instrumentalities to engage in such activities would be, in a very substantial measure, controlled or destroyed by the Federal government. New York City, as do other municipalities throughout the country, maintains numerous facilities which it deems "essential" to the proper conduct of life in a progressive community. Such facilities—water supply, surface and subway transit, public markets, wharves and piers, low cost housing, to name at random a few of many—are of vast importance to a great city. To authorize a Federal tax upon such activities would not merely burden the City—it would probably make their maintenance financially impossible. If such a result were not a direct interference with state sovereignty it is difficult to imagine what would be.

Factors identical with those above described have led this Court uniformly to exempt federal instrumentalities, regardless of their character, from state taxation. (See cases cited *supra*, pp. 3, 19-20.)

The inevitable conclusion is, to paraphrase the Chief Justice in his consideration of federal activities, "all ac-

tivities of [state] government * * * must stand on a parity with respect to their constitutional immunity from taxation" (*Graves* vs. *New York ex rel. O'Keefe,* 306 U. S. 466, 477 (1939)), and since federal activities of every nature are immune from state taxation, so all state activities, regardless of their nature, must be immune from federal taxation.

Since we have concluded that, under our form of government, it is beyond the power of Congress to tax *any* state property, activity or income, it necessarily follows that a "non-discriminatory" tax on such matters may not be laid by Congress. The subject of when a tax is "discriminatory" is too broad a question to discuss here. It is sufficient for us to point out that many taxes though doubtless discriminatory in operation have none-the-less been declared "non-discriminatory" in law. See *Rapid Transit Corp.* v. *New York,* 303 U. S. 573, 582 (1937). To give a single example, a tax upon the annual gross receipts of every class of corporation in excess of $750,000,000. might in law be "non-discriminatory", yet might operate upon few corporations other than the City of New York as a municipal corporation. The City of New York, with its annual expense budget of $875,000,000., might be crippled in its fiscal affairs and the entire balance of its governmental activities might be completely thrown out of gear by such a tax upon its revenues. Thus, in practice the mere fact that in form a tax laid upon state instrumentalities was "non-discriminatory" would offer no protection to the states at all. Moreover, as Petitioner has demonstrated (Brief on Reargument, pp. 5-14) discrimination has never been the test for determining governmental immunity from taxation.

Conclusion.

As we stated at the outset of this Brief, we have not addressed ourselves to the separate problem of whether or not Congress may constitutionally tax the individual recipients of state moneys, property or services. Such, in reality, is all this Court authorized in the *Allen* case, *supra*, when it held valid the imposition of an admission tax, to be paid by the spectator, upon attendance at a state-conducted football game.

Whatever devices Congress may contrive to tax property before it reaches the hands of a state (*Liggett & Meyers Co.* vs. *U. S.*, 299 U. S. 383 [1936]) or after it leaves the hands of a state (*Graves* v. *New York, ex rel. O'Keefe, supra*) should be separately considered as they arise in this Court.

The doctrine of sovereign immunity from taxation is fundamental in our form of constitutional government. The immunity of the States from federal taxation flows from the same basic principles as the Federal government's immunity from state taxation, and has been reiterated time and again by this Court. The Court should adhere to the rule of state immunity from federal taxation and should repudiate the unsound limitation placed upon it by the *South Carolina* case. That case, if it is to survive as precedent at all, should be limited in its application to its own facts and its doctrine should not extend to state activities other than the sale of liquor.

It is submitted that this Court should call a halt to the incursions upon state sovereignty which are bound to result unless the states receive from the Federal government the

same degree of immunity from taxes which the Federal government receives from the states.

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